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Travel and Entertainment Expense Deductions

Unreimbursed employee travel expenses are deductible but are subject to the 2% adjusted gross income (AGI) floor. If you are self-employed, the 2% floor does not apply. The types of deductible travel expenses are highlighted in the key to deductible travel and entertainment expenses at the beginning of this chapter. Generally, you must be away from home to deduct travel expenses on business trips. On one-day business trips within the general area of your employment, only transportation costs may be deducted; meals may not.

To support your travel expense deductions, keep records that comply with IRS rules as explained at ¶20.26. To avoid the 2% AGI floor, consider an “accountable” reimbursement arrangement of your travel expenses with your employer; see ¶20.31.

You report unreimbursed employee transportation and travel expenses on Form 2106 or on new short form 2106-EZ if you are not reimbursed by your company and you do not claim depreciation on a car used for business.

Unreimbursed expenses from Form 2106 or 2106-EZ are entered on Schedule A where they are subject to the 2% AGI floor.

An expense allowance for travel costs is not reported as income on Form W-2 if you substantiated the expenses to your employer and returned any unsubstantiated portion of the allowance; see ¶20.31 for details.

If you are self-employed, you deduct travel costs on Schedule C. The 2% AGI floor does not apply, but meal and entertainment expenses are subject to the 50% limitation.

Travel Expenses

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Travel Expenses

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¶20.1 Deduction Guide for Travel and Transportation Expenses

See ¶ 20.1 The following chart summarizes the rules for deducting travel expenses while “away from home” on business trips, and other deductible travel and transportation expenses; *see* ¶20.6 for when you are away from home. Generally, commuting expenses from your home to your place of business are not deductible; *see* ¶20.2. However, you may be able to claim a deduction for daily transportation expenses incurred in commuting to a temporary job location; *see* chart below and ¶20.2.



Key to Deductible Travel and Transportation Expenses

Your Travel Status—

Tax Rule—

Trips to see customers and clients

You may deduct your transportation expenses but not the cost of personal meals on one-day business trips within the general area of your tax home.

Two job locations for one employer in the same area

EXAMPLE—You work for two different employers in the city in which you live. You work about half of the time in each place—at one location in the morning and at the other in the afternoon.

You deduct transportation expenses from one location to the other. However, if, for personal reasons, such as the choice of a place for eating lunch, you do not go directly from one location to the other, you may deduct your transportation expenses only to the extent that they do not exceed the cost of going directly from the first location to the second. But say your employer has several locations in the same city, but you do not move from one location to another in the same day. You spend the entire day at one place. You may not deduct transportation expenses between your home and the various locations, even if you report to a different location each day.

Two different jobs in the same area

EXAMPLE—You live in Kansas City where you work. Most of the time you work a full work shift at your principal place of employment. Then you work a part-time shift for your second employer some distance away.

You may deduct the transportation expenses from one job to another within the same working day. But you may not claim the deduction if you return home after the first job and then, after supper, go to your second job.

Permanent job in an area other than where you have your residence

EXAMPLE—You live with your family in Chicago, but work in Milwaukee. During the week, you stay in a hotel in Milwaukee and eat meals in a restaurant. You return to your family in Chicago every weekend.

Milwaukee is your “home” for tax purposes; *see* ¶20.6. Thus, your expenses for traveling to Milwaukee and your meals and lodging there are personal, nondeductible expenses.

Temporary assignment in an area other than where you have your residence

EXAMPLE—You live in Kansas City where you work. You have been assigned to duty in Omaha for 60 days. Occasionally, you return to Kansas City on your days off, but most of the time you stay in Omaha.

You may deduct the necessary expenses for traveling from Kansas City to Omaha and returning to Kansas City after your temporary assignment is completed. You may also deduct expenses for meals and lodging (even for your days off) while you are in Omaha. As discussed at ¶20.9, deductions are not allowed on temporary assignments that are *expected* to last more than one year.

Weekend trip home from temporary assignment

EXAMPLE—Same facts as Example above except that you return home to Kansas City during the weekend.

You are not “away from home” while you are in Kansas City on your days off and your meals and lodging while you are there are not deductible. However, you may deduct your traveling expenses (including meals and lodging, if any) from Omaha to Kansas City and back if they are no more than the amount it would have cost you for your meals and lodging if you had stayed in Omaha. If they are more, your deduction is limited to the amount you would have spent in Omaha. If you retain your room in Omaha while in Kansas City, your expenses of returning to Kansas City on days off are deductible only to the extent of the amount you would have spent for your meals had you stayed in Omaha.

Temporary job location away from home where there are no living accommodations

EXAMPLE—You live and work in Chicago. You have been assigned for three months to a construction job located 20 miles outside Nashville. There are no living facilities near the job site and you have to stay at a hotel in Nashville.

Under these circumstances, your necessary expenses in getting to and from your temporary job are business expenses and not commuting expenses. If you were employed at the site for an indefinite period (¶20.9), then the costs of commuting would be nondeductible, regardless of the distance; *see* ¶20.2.

Taxi trips between customers’ locations

The cab fares are deductible; *see* ¶20.2.



Key to Deductible Travel and Transportation Expenses (Continued)

*Your Travel Status—**Tax Rule—***Seasonal jobs in different areas**

EXAMPLE—You live in Cincinnati where you work for eight months each year. You earn the greater share of your annual income from that job. For the remaining four months of the year, you work in Miami. When in Miami, you eat and sleep in a hotel. You have been working on both of these jobs for several years and expect to continue to do so.

You have two recurring seasonal places of employment. Cincinnati is your principal place of employment. You may deduct the costs of your traveling expenses while away from Cincinnati working at your minor place of employment in Miami, including meals and lodging in Miami.

Trailer home moved to different job sites

EXAMPLE—You are a construction welder. You live in a trailer which you move from city to city where you work on construction projects. You have no other established home.

You may not deduct your expenses for meals and lodging. Each place where you locate becomes your principal place of business and, therefore, you are not “away from home.”

Travel to school after work to take job-related courses

You may deduct travel costs if you meet the rules at ¶19.23.

Finding a new job in the same line of work

EXAMPLE—You live in New York. You travel to Chicago for an interview for a new position.

You may deduct the cost of the trip and living expenses in Chicago; see ¶19.7.

Convention trip

You may deduct costs of travel to a business convention under the rules of ¶20.12. If you are a delegate to a charitable or veterans' convention, you may claim a charitable deduction for the travel costs; see ¶14.4.

Trip to out-of-town college for educational courses

You deduct the cost of the trip if you meet the rules at ¶19.23.

Trip for health reasons

You may deduct the cost of the trip as a medical expense if you meet the rules at ¶17.9.

¶20.2 Commuting Expenses

The cost of travel between your home and place of work is generally not deductible, even if the work location is in a remote area not serviced by public transportation. Nor can you justify the deduction by showing you need a car for faster trips to work or for emergency trips. Travel from a union hall to an assigned job is also considered commuting. If you join a car pool, you may not deduct expenses of gasoline, repairs, or other costs of driving you and your passengers to work.

According to the IRS, if you install a telephone in your car and make calls to clients or business associates while driving to your office, you are still commuting and your expenses are not deductible. Similarly, the deduction is not allowed if you drive passengers to work and discuss business. However, an IRS and Tax Court decision that barred police captains' costs of driving their specially equipped cars to and from the stationhouse was reversed by an appeals court.

Deductible commuting expenses. The IRS allows these exceptions to its blanket ban on commuting expense deductions.

If you are on a business trip out of town, you may deduct taxi fares or other transportation costs from your hotel to the first business call of the day and all other transportation costs between business calls.

If you use your car to carry tools to work, you may deduct transportation costs where you can prove that they were incurred in addition to the ordinary, nondeductible commuting expenses. The deduction will be allowed even if you would use a car in any event to commute; *see* the Examples below.

EXAMPLES

1. Jones commuted to and from work by public transportation before he had to carry tools. Public transportation cost \$2 per day to commute to and from work. When he had to use the car to carry the tools, the cost of driving was \$3 a day and \$5 a day to rent a trailer to carry the tools. Jones may deduct only the cost of renting the trailer. The IRS does not allow a deduction for the additional \$1 a day cost of operating the car. It is not considered related to the carrying of the tools. It is treated as part of the cost of commuting which is not deductible.
2. Same facts as above, but Jones does not rent a trailer. He uses the car trunk to store his tools. He may not claim a deduction because he incurs no additional cost for carrying the tools.
3. Smith uses his car regardless of the need to transport tools. He rents a trailer for \$5 a day to carry tools. He may deduct \$5 a day under the "additional-cost" rule.

Commuting to a temporary place of work. Whether you can deduct commuting expenses to a temporary place of work may depend on the location of the temporary assignment and whether you have a regular place of business or a home office which is your principal place of business. According to the IRS, if the temporary location is within the metropolitan area where you live and usually work, you must show either that you have a regular place of business outside your home, or that your principal place of business is your office in your home. If the temporary location is outside the metropolitan area, you may deduct commuting expenses to the temporary location without having to meet either the regular place of business or home office test.

Given the difficulty of proving that a home office is the principal place of business (¶19.13), self-employed persons such as plumbers, electricians, and salespersons who do not have a regular place of business outside the home are prevented from deducting commuting costs *within* the metropolitan area of the home. For example, the IRS barred a self-employed lumberjack who did not have an office outside his home from deducting the cost of driving from home to the first logging site of the day and returning home from the last site.

What is a temporary place of work? A temporary place of work is any location where you perform services on an irregular basis or for a short-term period, generally a few days or weeks. If you are on a temporary job that lasts longer, it is important to show that the job started out as a temporary assignment and that factors beyond your control extended the time and that you looked for work closer to home.



Self-Employed Person's Office at Home

If you are self-employed and your regular office is outside your home, you may not deduct the cost of commuting to the office or from that office to your home even if you work at home at a second job. However, in several cases, the Tax Court allowed self-employed persons whose home office was their principal place of business (¶19.13) to deduct travel costs beginning with the first business call of the day. The IRS agrees with this approach.

¶20.3 Overnight-Sleep Test Limits Deduction of Meal Costs

The overnight-sleep rule prevents the deduction of meal costs on one-day business trips. To be deductible, meal costs must be incurred on a business trip that lasts longer than a regular working day (but not necessarily 24 hours) and requires time off to sleep (not just to eat or rest) before returning home. Taking a nap in a parked car off the road does not meet the overnight-sleep test.

EXAMPLES

1. A New Yorker flies to Washington, D.C., which is about 250 miles away, to see a client. He arrives at noon, eats lunch, and then visits the client. He flies back to New York. He may deduct the cost of the plane fare, but not the cost of the lunch. He was not away overnight nor was he required to take time out to sleep before returning home.
2. Same facts as above except he sleeps overnight in a Washington hotel. He eats breakfast there, and then sees another client and returns home to New York in the afternoon. He may deduct not only the cost of the plane fare but also the cost of the meals while on the trip and the cost of the hotel, since he was away overnight.
3. A trucker's run is from Seattle to Portland and back. He leaves at about 2:00 A.M. and returns to Seattle the same day, getting in at about 6:00 P.M. While in Portland, he is released from duty for about four hours layover time to get necessary sleep before returning to Seattle. He may deduct the cost of meals because he is released at a layover location to obtain necessary sleep. Official release from duty, however, is not a prerequisite for satisfying the sleep or rest test.

Several courts held that the IRS rule was unreasonable and outdated in the world of supersonic travel, and they would have allowed the New Yorker on the one-day trip to Washington, D.C., to deduct the cost of his lunch. The Supreme Court disagreed and upheld the IRS rule as a fair administrative approach.

Meal costs during overtime. Such costs are not deductible if you are not away from your place of business. Thus, for example, a resident physician could not deduct the cost of meals and sleeping quarters at the hospital during overnight or weekend duty.

¶20.4 IRS Meal Allowance

If you find it difficult to keep records of meal costs while away from home on business trips, you may prefer to claim an IRS meal allowance. The allowance covers, in addition to meals, incidental expenses, such as laundry and tips for services. Self-employed individuals may claim the allowance as well as employees who are not reimbursed for meals under an "accountable" plan; see ¶20.31.

1996 Meal Allowance. For travel within the continental U.S., the daily allowance for 1996 is usually \$26 per day except that in certain high-cost areas designated by the government, the allowance may be \$30, \$34, or \$38 per day. The high-cost areas are generally major metropolitan cities or resort areas. See below for the different meal allowance rates that apply for business travel in 1996. Also see IRS Publication 463 for allowance rate tables.

For travel in Alaska, Hawaii, or other areas outside the continental U.S., an allowance for each location is shown in government tables.

You must keep a record of the time, place, and business purpose of the trips. As long as you have this proof, you may claim the allowance even if your actual costs are less than the allowance.



Meal Allowance Rates for 1996

If you traveled on business between January 1, 1996, and March 31, 1996, there may be a different rate than for travel on or after April 1, 1996. See the following explanation of Tables I and II for locations that qualify for a meal allowance rate over the basic \$26 rate.

Table I and Table II. For business trips within the continental U.S., a daily allowance of either \$26, \$30, \$34, or \$38 per day may be claimed depending on the location. See Table I on pages 324 and 325 for a list of the cities that qualify for rates over \$26 per day for the period April 1, 1996–December 31, 1996.

The allowance shown in Table I for a particular city also applies for January, February, and March of 1996 if the city is not highlighted. However, if the city is highlighted, this means that a different allowance applies for travel during the first three months of 1996. If the allowance for the first three months is over \$26, it is shown in Table II on page 326.

If a city qualifies for an allowance over \$26 for January–March 1996, but not for the rest of the year, it will be shown on Table II only. If a city is not shown on either Table I or Table II, the allowance is \$26 per day for the entire year.

EXAMPLES

1. You took two business trips to Mobile, Alabama in 1996, one in February and one in July. On Table I, a \$34-per-day allowance applies to Mobile for travel on or after April 1, 1996. Since Mobile is *not* highlighted, the \$34 rate also applies to travel before April 1, 1996. Both trips qualify for the \$34 meal allowance.
2. Same as Example 1 except that the trips were to Huntsville, Alabama, instead of Mobile. Table I shows the \$30 allowance for travel to Huntsville on or after April 1, 1996. Since Huntsville is highlighted on Table I, a different allowance applies for travel before April 1. Table II shows a \$34 allowance for Huntsville for travel from January 1–March 31, 1996.

Transportation industry workers. Employees or self-employed persons in the *transportation industry* may elect to claim a meal allowance of \$32 per day for all travel within the continental U.S. instead of applying the \$26, \$30, \$34, or \$38 rate on a trip-by-trip basis. Also, an allowance of \$36 per day may be elected for all travel outside the continental U.S.

Table I: Locations Eligible for \$30, \$34, or \$38 a Day Meal Allowance for Travel April 1 – December 31, 1996*

The allowance applies to the county, parish, borough, and military installation surrounding the city shown. See IRS Publication 463 for a full list of counties. Any changes to the list will be in the Supplement.

STATE	\$30	\$34	\$38
ALABAMA	Birmingham, Gulf Shores, HUNTSVILLE , and Sheffield	Mobile	
ARIZONA	Flagstaff, Prescott, Sierra Vista, and Tucson	GRAND CANYON NAT'L PARK AND KAIBAB NAT'L FOREST IF WITHIN COCONINO COUNTY , and Phoenix/Scottsdale	
ARKANSAS	Hot Springs, Little Rock, and Texarkana		
CALIFORNIA	Chico, El Centro, Eureka, MERCED, SANTA BARBARA, STOCKTON , Vallejo, West Sacramento, and Yuba City	Bridgeport, DEATH VALLEY, FRESNO , Modesto, Monterey, Napa, OAKLAND , Redding, SACRAMENTO, SAN DIEGO , San Luis Obispo, SAN MATEO/REDWOOD CITY , Santa Cruz, SANTA ROSA , and Visalia	Gualala/Point Arena, Los Angeles, ONTARIO/VICTORVILLE/BARSTOW, PALM SPRINGS , Palo Alto/San Jose, San Francisco, South Lake Tahoe, Tahoe City, and Yosemite Nat'l Park
COLORADO	Glenwood Springs and Grand Junction	Boulder, DENVER , Durango, Steamboat Springs, and TELLURIDE	Aspen, Keystone/Silverthorne, and Vail
CONNECTICUT	NEW HAVEN and PUTNAM/DANIELSON	Bridgeport/Danbury, HARTFORD, NEW LONDON/GROTON , and SALISBURY	
DELAWARE	DOVER and LEWES	Wilmington	
DISTRICT OF COLUMBIA			Washington, D.C.
FLORIDA	Altamonte Springs, BRADENTON, COCOA BEACH , Daytona Beach, FORT LAUDERDALE, FORT MEYERS , Fort Walton Beach, GAINESVILLE , Jacksonville, Kissimmee, LAKELAND, OCALA , Pensacola, Punta Gorda, St. Augustine, Sarasota, Stuart, Tallahassee, and WEST PALM BEACH	ORLANDO and Naples	Key West and Miami
GEORGIA	ATHENS, AUGUSTA, COLUMBUS , and CONYERS	ATLANTA	
IDAHO	BOISE , Idaho Falls, McCall, Pocatello, SANDPOINT , and Stanley		KETCHUM/SUN VALLEY
ILLINOIS	Alton, Champaign/Urbana, Decatur, EAST ST. LOUIS, JOLIET , and Springfield	PEORIA	Chicago and ROCKFORD
INDIANA	Bloomington/Crane, Columbus, Evansville, Gary/ MERRILLVILLE, INDIANAPOLIS , Lafayette, and Nashville		Carmel
IOWA	Bettendorf/Davenport and Cedar Rapids		
KANSAS	TOPEKA	Kansas City and WICHITA	
KENTUCKY	Bowling Green, Florence, Lexington, LONDON , and Paducah	Covington and Louisville	
LOUISIANA	Alexandria, Baton Rouge, GONZALES , Lafayette, and Shreveport	New Orleans	
MAINE	AUBURN , Augusta, Bangor, BAR HARBOR , Kennebunk/Sanford, and Rockport	Kittery and PORTLAND	
MARYLAND	Easton, FREDERICK, GRASONVILLE , Hagerstown, LEXINGTON PARK/ST. INIGOE/LEONARDTOWN, LUSBY , Salisbury, and Waldorf		Annapolis, Baltimore, Columbia, the counties of Montgomery and Prince Georges, and Ocean City
MASSACHUSETTS	Quincy and Springfield	Andover, CAMBRIDGE/LOWELL , Hyannis, and PITTSFIELD	Boston and Martha's Vineyard/Nantucket
MICHIGAN	Ann Arbor, BAY CITY , Charlevoix, GAYLORD , Kalamazoo, Lansing/East Lansing, LELAND, MONROE, PORT HURON , St. Joseph/Benton Harbor/Niles, and Traverse City	GRAND RAPIDS and PONTIAC/TROY	Detroit and Mackinac Island
MINNESOTA	Brainerd, Grand Rapids, Rochester, and St. Cloud	Duluth	MINNEAPOLIS/ST. PAUL
MISSISSIPPI	Biloxi/Gulfport/Pascagoula/Bay St. Louis and NATCHEZ	JACKSON and RIDGELAND	

*If not highlighted, the allowance shown also applies from January 1 – March 31. If highlighted, a different allowance applies for travel before April 1, 1996; see Table II.

Table I: Locations Eligible for \$30, \$34, or \$38 a Day Meal Allowance for Travel April 1 – December 31, 1996*

The allowance applies to the county, parish, borough, and military installation surrounding the city shown. See IRS Publication 463 for a full list of counties. Any changes to the list will be in the Supplement.

STATE	\$30	\$34	\$38
MISSOURI	Branson, CAPE GIRARDEAU, COLUMBIA, JEFFERSON CITY, LAKE OZARK, Osage Beach, and Springfield	Kansas City	St. Louis
NEBRASKA	KEARNEY, LINCOLN, and Omaha		
NEVADA	WINNEMUCCA	INCLINE VILLAGE, LAS VEGAS, and RENO	Stateline
NEW HAMPSHIRE	Laconia	Conway and Portsmouth/Newington	HANOVER
NEW JERSEY	FLEMINGTON, Millville, and Tom's River	Belle Mead, Camden, MOORESTOWN, Freehold/Eaton-town, Ocean City/Cape May, and Princeton/Trenton	Atlantic City, Edison, Newark, and Parsippany/Dover
NEW MEXICO	Farmington and Los Alamos	Albuquerque and Taos	SANTA FE
NEW YORK	CORNING, Kingston, Lake Placid, Monticello, Niagara Falls, PALISADES/NYACK, Plattsburgh, Poughkeepsie, SCHENECTADY, SYRACUSE, Utica, and Watertown	Albany, Binghamton, Glens Falls, SARATOGA SPRINGS, and Troy	BUFFALO, New York City, Long Island, ROCHESTER, and White Plains
NORTH CAROLINA	Duck/Outer Banks, Greensboro/High Point, Greenville, WILMINGTON, and Winston-Salem	ASHEVILLE, Charlotte, and Research Park/Raleigh/Durham/Chapel Hill	
NORTH DAKOTA	Bismarck/Mandan	FARGO	
OHIO	CAMBRIDGE, CINCINNATI/EVENDALE, COLUMBUS, Dayton/Fairborn, Elyria, GENEVA, MARTIN'S FERRY/BELLAIRE, Port Clinton/Oak-harbor, Sandusky, Springfield, Toledo, and Warren	Akron	Cleveland
OKLAHOMA	OKLAHOMA CITY and Tulsa/Bartlesville		
OREGON	Ashland/Medford, Bend, Eugene, GOLD BEACH, and Seaside	Beaverton, LINCOLN CITY/NEWPORT, and PORTLAND	
PENNSYLVANIA	ALTOONA, Bloomsburg, DU BOIS, Erie, Gettysburg, Lancaster, Shippingport/Beavers Fall, State College, Stroudsburg, Warminster, Williamsport, and York	Allentown, CHESTER/RADNOR, Harrisburg, King of Prussia/Ft. Washington, Philadelphia, VALLEY FORGE/MALVERN, and WILKES-BARRE	PITTSBURGH
RHODE ISLAND		BLOCK ISLAND, East Greenwich, and QUONSET POINT	Newport and PROVIDENCE
SOUTH CAROLINA	AIKEN, CHARLESTON, Columbia, FLORENCE, and Myrtle Beach	GREENVILLE	HILTON HEAD
SOUTH DAKOTA	Rapid City and Sioux Falls		
TENNESSEE	CHATTANOOGA, JACKSON, Johnson City, Kingsport, and MEMPHIS	GATLINBURG, KNOXVILLE, and NASHVILLE	
TEXAS	Amarillo, Beaumont, El Paso, Lajitas, LUBBOCK, McALLEN, SAN ANTONIO, Texarkana, and WACO	Austin, CORPUS CHRISTI/INGLESIDE, and HOUSTON	DALLAS/FORT WORTH and Galveston
UTAH	Bullfrog, Cedar City, and MOAB	PROVO and SALT LAKE CITY/OGDEN	PARK CITY
VERMONT	Burlington, Middlebury, Rutland, and White River Junction		
VIRGINIA	Fredericksburg, Lynchburg, and Manassas/Manassas Park	Chesapeake, Hampton, Newport News, Norfolk, Portsmouth, ROANOKE, Virginia Beach, Williamsburg, WINTER-GREEN, and Yorktown	Alexandria, Charlottesville, Fairfax, Falls Church, and RICHMOND. Also, counties of Arlington, Fairfax, and Loudoun
WASHINGTON	BELLINGHAM, Kelso/Longview, OCEAN SHORES, PORT ANGELES, Port Townsend, RICHLAND, Spokane, TACOMA, TUMWATER/OLYMPIA, VANCOUVER, and Yakima	ANACORTES/MT. VERNON/WHIDBEY ISLAND, FRIDAY HARBOR, Lynwood/Everett, and SEATTLE	
WEST VIRGINIA	Harpers Ferry		
WISCONSIN	Appleton, Eau Claire, GREEN BAY, La Crosse, LAKE GENEVA, Madison, Milwaukee, Oshkosh, Racine/Kenosha, SHEBOYGAN/PLYMOUTH, STEVENS POINT, SUPERIOR, and WAUSAU	Brookfield and Wisconsin Dells	
WYOMING	Casper, Cheyenne, and Rock Springs		JACKSON

*If not highlighted, the allowance shown also applies from January 1 – March 31. If highlighted, a different allowance applies for travel before April 1, 1996; see Table II.

Table II: Locations Eligible for \$30, \$34, or \$38 a Day Meal Allowance for Travel on or after January 1, 1996, but before April 1, 1996*

The allowance applies to the county, parish, borough, and military installation surrounding the city shown. See IRS Publication 463 for a full list of counties. Any changes to the list will be in the Supplement.

STATE	\$30	\$34	\$38
ALABAMA		Huntsville	
ARIZONA	Casa Grande, Chinle, and Grand Canyon Nat'l Park/Kaibab Nat'l Forest if within Coconino County		
CALIFORNIA	Clearlake and Fresno	Merced, Ontario/Victorville/Barstow, Palm Springs, Santa Barbara, and Stockton	Death Valley, Oakland, San Mateo/Redwood City, Sacramento, San Diego, and Santa Rosa
COLORADO	Pagosa Springs		Denver
CONNECTICUT	New London/Groton and Vernon	New Haven	Hartford and Salisbury
DELAWARE		Lewes	
FLORIDA	Fort Pierce, Orlando, Panama City, and Tampa/St. Petersburg	Cocoa Beach, Fort Lauderdale, Fort Meyers, Gainesville, and West Palm Beach	
GEORGIA	Albany, Macon, and Savannah		Atlanta and Norcross/Lawrenceville
IDAHO		Boise and Ketchum/Sun Valley	
ILLINOIS	Bloomington and Peoria	Rockford	
INDIANA	Fort Wayne and Greenwood	Indianapolis	
IOWA	Des Moines, Dubuque, Iowa City and Waterloo		
KANSAS	Wichita		
LOUISIANA	Monroe and Slidell		
MAINE	Bath, Portland, and Wiscasset	Bar Harbor	
MARYLAND	Tower Garden on Bay	Frederick and Lusby	
MASSACHUSETTS	Pittsfield, South Deerfield/Greenfield, and Worcester		Cambridge/Lowell
MICHIGAN	Battle Creek, Flint, Grand Rapids, and Saginaw	Port Huron	Pontiac/Troy
MINNESOTA	Bemidji and Mendota Heights	Minneapolis/St. Paul	
MISSISSIPPI	Jackson and Vicksburg		Ridgeland
MISSOURI		Lake Ozark	
NEVADA	Elko and Reno		Las Vegas
NEW HAMPSHIRE	Manchester	Cornish and Hanover	
NEW JERSEY			Moorestown
NEW MEXICO	Las Cruces/White Sands	Santa Fe	
NEW YORK	Catskill, Elmira, Ithaca, Jamestown, Watkins Glen, and West Point	Buffalo, Corning, Palisades/Nyack, Rochester, Schenectady, and Syracuse	Saratoga Springs
NORTH CAROLINA	Asheville and Morehead City		
NORTH DAKOTA	Fargo		
OHIO		Cincinnati/Evendale and Columbus	
OREGON	Lincoln City/Newport and Portland		
PENNSYLVANIA	Lebanon, Mechanicsburg, Reading, Scranton, Somerset, and Wilkes-Barre	Pittsburgh	Chester/Radnor and Valley Forge/Malvern
RHODE ISLAND		Providence	
SOUTH CAROLINA		Charleston and Hilton Head	
TENNESSEE	Gatlinburg, Bristol, Knoxville, and Nashville	Memphis	
TEXAS	Brownsville, Corpus Christi/Ingelside, Denton, Laredo, and Plano	Dallas/Fort Worth and San Antonio	Houston
UTAH	Provo and Salt Lake City/Ogden		
VIRGINIA	Roanoke, Wallops Island, and Warrenton/Amissville	Richmond	Wintergreen
WASHINGTON	Anacortes/Mt. Vernon, Bremerton, and Whidbey Island	Bellingham, Port Angeles, Richland, Tumwater/Olympia, and Vancouver	Friday Harbor and Seattle
WEST VIRGINIA	Charleston, Martinsburg, Morgantown, and Parkersburg		
WISCONSIN		Lake Geneva	
WYOMING		Jackson	

*Other than those not highlighted in Table I. Locations highlighted in Table I that do not appear here are eligible for a meal allowance of only \$26 per day for travel on or after January 1, 1996, but before April 1, 1996.

Claiming the allowance. The allowance is allocated for the first and last day of a trip. The day is divided into four six-hour periods, starting at midnight. For each six-hour period that you are away, you are entitled to 25% of the allowance. If you start your business trip between midnight and 6 A.M., you are considered to be away for the entire day and may claim the full day allowance for the first day. If you start between 6 A.M. and noon, you claim 75% of the allowance for the first day; if you start between noon and 6 P.M., you claim 50% of the allowance for the first day, and 25% if you leave between 6 P.M. and midnight.

If you are an employee and claim a deduction based on the allowance, you must reduce the deduction by 50% on Form 2106 or Form 2106-EZ. Furthermore, if you are an employee, the balance, when added to your other miscellaneous deductions, is subject to the 2% AGI floor on Schedule A. If you are self-employed, the deduction for meals is claimed on Schedule C, where it is subject only to the 50% reduction; see ¶40.5.

Reimbursement plans. If your employer has an “accountable” reimbursement plan (¶20.31), and you are reimbursed for meals up to the allowable rate, the reimbursement will not be reported as income on your Form W-2.

Deducting Travel Expenses
Away From Home

	See ¶
Business trip deductions	20.5
When are you away from home?	20.6
Fixing a tax home if you work in different locations	20.7
Tax home of married couple working in different cities	20.8
Deducting living costs on temporary assignment	20.9

¶20.5 Business Trip Deductions

The following expenses of a business trip *away from home* (¶20.6) are deductible if not reimbursed by your employer:

- Plane, railroad, taxi, and other transportation fares.
- Hotel and lodging expenses.
- Meal costs. Only 50% of the cost of the meal is deductible. The business discussion test of ¶20.16 does not apply to meal costs on business trips provided you eat alone or with your family or personal acquaintances.
- Tips, telephone, and telegraph costs.
- Laundry and cleaning expenses.
- Baggage charges (including insurance).
- Cab fares or other costs of transportation to and from the airport or station and your hotel. Also deductible are cab fares or other

- transportation costs, beginning with your first business call of the day, of getting from one customer to another, or from one place of business to another.
- Travel costs to find a new job are deductible; see ¶19.7.
 - Entertainment expenses incurred while traveling away from home are deductible under the rules at ¶20.6.

Cruise ship. If you travel by cruise ship on a business trip, your deductible cruise costs are limited to twice the highest federal *per diem* rate for travel in the United States on that date times days in transit.

EXAMPLE

You sail to Europe on business. The highest *per diem* federal rate is \$202 and the trip lasts five days. The maximum deduction for the cost of the trip is \$2,020 (2 × \$202 × 5). The double *per diem* rule applies without regard to the 50% limit on meal costs if meals are not separately stated in your bill. If a separate amount for meals or entertainment is included, such amount must be reduced by 50%.

The *per diem* limitation does not apply to cruise ship convention costs that are deductible up to \$2,000 a year, if all the ports of call are in the U.S. or U.S. possessions and if the ship is registered in the United States; see ¶20.14. The *per diem* rate also does not apply if the expense comes within an exception to the 50% cost limit rule explained at ¶20.24.

Important: Record-keeping requirements. See the section beginning at ¶20.26 for record-keeping rules to support a deduction for unreimbursed travel expenses or to avoid being taxed on employer reimbursements.

¶20.6 When Are You Away
From Home?

You have to meet the “away from home” test to deduct the cost of meals and lodging while traveling.



Tax Home Defined

For travel expense purposes, your home is your place of business, employment, or post of duty, regardless of where you maintain your family residence. This tax home includes the entire city or general area of your business premises or place of employment. The area of your residence may be your tax home if your job requires you to work at widely scattered locations, you have no fixed place of work, and your residence is in a location economically suited to your work.

EXAMPLES

1. Your residence is in a suburb within commuting distance of New York City where you work full time. Your personal home and tax home are the same, that is, within the metropolitan area of New York City. You are away from home when you leave this area, say for Philadelphia. Meals and lodging are deductible only if you meet the overnight-sleep test; see ¶20.3.
2. Your residence is in New York City, but you work in Baltimore. Your tax home is Baltimore; you may not deduct living expenses there. But you may deduct travel expenses on a temporary assignment to New York City even while living at your home there.
3. A construction worker works for a utility company on construction sites in a 12-state area. Assignments are sent from his employer's regional office; he is not required to report to the office. The IRS ruled that his residence, which is in a city in the 12-state area, is his tax home.

Are you constantly on the road? If you are, an IRS agent may disallow your travel deductions on the grounds that your tax home is wherever you work; thus, you are never “away from home.” If your deduction is questioned, you may be able to show that your tax home is the area of your residence. If you meet these three tests, the IRS will treat your residence as your tax home: (1) you do some work in the vicinity of your residence, house, apartment, or room and live there while performing services in the area; (2) you have mortgage expenses or pay rent for the residence while away on the road; (3) the residence is in an area where you were raised or lived for a long time, or a member of your immediate family such as your parent or child lives in the residence, or you frequently return there.

According to the IRS, if you meet only two of these three tests, it will decide on a case-by-case basis if your residence is your tax home. If you meet less than two of the tests, the IRS will not allow a deduction; each of your work locations is treated as your tax home.

If you live in a trailer at each job assignment and have no other home, each job location is your principal place of business and you are “not away from home.”

Permanent duty station of servicemembers. The Supreme Court held that a member of the Armed Forces is not away from home when he or she is at a permanent duty station. This is true whether or not it is feasible or even permissible for the servicemember's family to live with him or her.

¶20.7 Fixing a Tax Home If You Work in Different Locations

If you regularly work in two or more separate areas, your tax home is the area of your principal place of business or employment. You are away from home when you are away from the area of your principal place of business or employment. Therefore, you may deduct your transportation costs to and from your minor place of business and your living costs there.

Professional sports players, coaches, and managers. When the only business of such persons is the professional sport, their home is the “club town.” But if they are in another business in addition to their professional playing, how much time is spent and how much is earned at each place determines whether their club's hometown or the place of their off-season business is their tax home. If it is the club's hometown, they deduct travel and living expenses while away from that town—including the time they are where the second business is. (If the second place is where their families also live, they may not deduct the families' expenses there.) If the town where the other business is located is the tax home, then expenses in the club's hometown may be deducted.

Airline pilots. It is important for airline pilots who fly in and out of various locations to determine a tax home for income and deduction purposes. Generally, the IRS considers an airline pilot's tax home to be the airport at which the pilot is regularly based. For example, in one case the IRS barred a pilot from claiming the foreign earned income exclusion (¶36.1) because his tax home was deemed to be his base in New York, rather than in London where he and his wife actually lived.



Determining Your Principal Place of Business

A principal place of business or employment is determined by comparing: (1) the time ordinarily spent working in each area; (2) the degree of your business activity in each area; and (3) the amount of your income from each area.

The relative importance of each fact will vary, depending on the facts of a particular case. For example, where there are no substantial differences between incomes earned in two places of employment, your tax home is probably the area in which you spend more of your time. Where there are substantial income differences, your tax home is probably the area in which you earn more of your income.

EXAMPLES

1. Sherman lived in Worcester, Mass., where he managed a factory. He opened his own sales agency in New York. He continued to manage the factory and spent considerable time in Worcester. The larger part of his income came from the New York business. However, he was allowed to treat New York as his minor place of business and to deduct his travel expenses to New York and his living expenses there because he spent most of his time in Worcester and his income there was substantial.
2. Benson, a consulting engineer, maintained a combination residence-business office in a home he owned in New York. He also taught four days a week at a Technological Institute in West Virginia under a temporary nine-month appointment. He spent three-day weekends, holidays, and part of the summer at his New York address. At the Institute, he rented a room in the student union building. The IRS disallowed transportation expenses between New York and West Virginia and meals and lodging

there as not incurred while away from home. The Tax Court disagreed. A taxpayer may have more than one occupation in more than one city. When his occupations require him to spend a substantial amount of time in each place, he may deduct his travel expenses, including meals and lodging, at the place away from his permanent residence. That Benson's teaching salary happened to exceed his income from his private practice does not change the result.

¶20.8 Tax Home of Married Couple Working in Different Cities

When a husband and wife work and live in different cities during the week, one of them may seek to deduct travel expenses away from home. Such deductions have generally been disallowed, but courts have allowed some exceptions. Although for common law purposes the domicile of the husband may be the domicile of the wife, for tax purposes when each spouse works in a different city, each may have a separate tax home.

EXAMPLES

1. Robert worked in Wilmington, Delaware; his wife, Margaret, worked in New York City. During the weekend, she traveled to Wilmington and deducted, as travel expenses away from home, her living costs in New York and weekend travel expenses to Wilmington. She argued that because she and her husband filed a joint return, they were a single taxable unit, and the tax home of this unit was Wilmington where her husband lived. The deduction was disallowed. That a couple can file a joint return does not give them deductions that are not otherwise available to them as individuals. Margaret's tax home was New York where she worked. Therefore, her expenses there are not deductible. And, as the weekend trips to Wilmington had no relationship to her job, they, too, are not deductible.
2. Hundt and his wife lived in Arlington, Va., but he wrote and directed films in various parts of the country. He wrote screenplays either at his Arlington home or on location, but most of his business came from New York City, where he lived in hotels. One year, he spent 175 days in New York City on business and rented an apartment for \$1,200 because it was cheaper than a hotel. He deducted half the annual rent for the New York apartment, the costs of traveling between Arlington and New York, and the cost of meals in New York. The IRS disallowed the expenses, finding New York to be his tax home. The court disagreed. Arlington was Hundt's tax home because (1) part of his income came from his creative writing in Arlington; and (2) his travel to other parts of the country was temporary. The fact that most of his income came from New York did not make New York his tax home.

¶20.9 Deducting Living Costs on Temporary Assignment

A business trip or job assignment away from home (¶20.6) at a single location may last a few days, weeks, or months. If your assignment is considered *temporary*, you may deduct living costs away from home. An assignment lasting *more than one year* is indefinite if you realistically expected it to last that long when you started the assignment, and you may not deduct your living costs of such an assignment. According to the IRS, the one-year test does not mean that expenses incurred during a stay of up to one year are deductible. You can be away for less than a year and still be barred from claiming a deduction if at the time you started the assignment you *realistically expected* it to last for more than a year; see the Examples below.

EXAMPLES

1. You are on a job assignment away from home in a *single* location that is expected to last (and it does in fact last) for one year or less. The IRS will treat the employment as temporary, unless facts and circumstances indicate otherwise. Expenses are deductible.
2. You are sent on a job assignment away from home at a *single* location. You expected that the job would last 18 months. However, due to financial difficulties you were transferred home after 11 months. Even though your assignment actually lasted for less than one year the IRS treats the employment as indefinite because you realistically expected it to last more than one year. Thus, your travel and living expenses while away from home are not deductible.
3. You are sent on a job assignment away from home at a *single* location. You expected that the job would last only nine months. However, due to changed circumstances occurring after eight months, you were asked to remain on the assignment for six more months. The IRS treats the assignment as temporary for eight months, and indefinite for the remaining time you are away from home. Thus, travel and living expenses you paid or incurred during the first eight months are deductible; expenses paid or incurred thereafter are not.

Deductible costs on temporary trip. While on a temporary job assignment *expected* to last a year or less, you may deduct the cost of meals and lodging there, even for your days off. If you return home, say for weekends, your living expenses at home are not deductible. You may deduct travel expenses, meals, and lodging en route between your home and your job assignment provided they do not exceed your living expenses had you stayed at the temporary job location. If you keep a hotel room at the temporary location while you return home, you may deduct your round-trip expenses for the trip home only up to the amount you would have spent for meals had you stayed at the temporary workplace.



Taking Your Family with You

If you take your family with you to a temporary job site, an IRS agent may argue that this is evidence that you considered the assignment to be indefinite. In the Example below, however, such a move was not considered detrimental to a deduction of living expenses at the job location.

EXAMPLE

Michaels, a cost analyst for Boeing, lived in Seattle. He traveled for Boeing, but was generally not away from home for more than five weeks. Michaels agreed to go to Los Angeles for a year to service Boeing's suppliers in that area. He rented his Seattle house and brought his family with him to Los Angeles. Ten months later, Boeing opened a permanent office in Los Angeles and asked Michaels to remain there permanently. Michaels argued that his expenses for food and lodging during the 10-month period were deductible as "away from home" expenses. The IRS contended that the Los Angeles assignment was for an indefinite period.

The Tax Court sided with Michaels. He was told that the stay was for a year only. He leased his Seattle house to a tenant for one year, planning to return to it. He regarded his work in Los Angeles as temporary until Boeing changed its plans. The one-year period justified his taking the family but did not alter the temporary nature of the assignment.

No regular job where you live. That you do not have regular employment where you live may prevent a deduction of living costs at a temporary job in another city. The IRS may disallow the deduction on the grounds that the expenses are not incurred while away from home; the temporary job site is the tax home.

Deducting Expenses of a Business-Vacation Trip

Business-vacation trips within the United States
 Business-vacation trips outside the United States
 Deducting expenses of business conventions
 Travel expenses of a spouse or dependents
 Restrictions on foreign conventions and cruises

See ¶

20.10
 20.11
 20.12
 20.13
 20.14

¶20.10

Business-Vacation Trips Within the United States

On a business trip to a resort area, you may also spend time vacationing. If the *primary purpose* of the trip is to transact business and the area is within the United States (50 states and District of Columbia) you may deduct all of the costs of your transportation to and from the area, lodging, and 50% of meal expenses, even if you do spend time vacationing. If the main purpose of the trip was personal, you may not deduct any part of your travel costs to and from the area. The amount of time spent on business as opposed to sightseeing or personal visits is the most important issue in determining your primary purpose. Regardless of the primary purpose of your trip, you are allowed to deduct expenses related to the business you transacted while in the area.

No deductions will be allowed if you attend a convention or seminar where you are given videotapes to view at your own convenience and no other business-related activities or lectures occur during the convention. The trip is considered a vacation.



Primary Business Purpose

If your return is examined, proving business purpose depends on presenting evidence to convince an examining agent that the trip, despite your vacationing, was planned primarily to transact business. Keep a log or diary to substantiate business activities.

If your trip is primarily for business, and while at the business destination you extend your stay for a few days for nonbusiness reasons, such as to visit relatives, you deduct travel expenses to and from the business destination.

EXAMPLE

You work in Atlanta and make a business trip to New Orleans. You stay in New Orleans for six days and your total costs, including round-trip transportation to and from New Orleans, meals, and lodging, is \$600, which you may deduct subject to the 50% limit for meals. If, on your way home, you spend three days in Mobile visiting relatives and incur an additional \$200 in travel costs, your deduction is limited to the \$600 (less 50% of meals) you would have spent had you gone home directly from New Orleans.

Reimbursement for weekend travel. If your employer extends your business trip over a weekend to take advantage of discount airfares which require a Saturday night stayover, you may deduct the cost of meals, lodging, and other incidental expenses incurred for the additional night. The reason for the stayover has a business purpose: to cut travel costs. If your employer pays for the expenses directly or if you are reimbursed under an accountable plan (¶20.31), the payment is not taxable to you.

¶20.11 Business-Vacation Trips Outside the United States

On a business trip abroad, you may deduct your travel expenses (50% of meals), even though you take time out to vacation, provided you can prove: (1) the primary purpose of the trip was business; and (2) you did not have control over the assignment of the trip.

If the IRS determines that you were primarily on vacation, it will disallow all travel costs except for costs directly related to your business in the area such as registration fees at a foreign business convention; see ¶20.14.

Fixing the date of the trip does not mean that you had control over the assignment. IRS regulations assume that when you travel for your company under a reimbursement or allowance arrangement, you do not control the trip arrangements, provided also that you are not: (1) a managing executive of the company; (2) related to your employer; or (3) have 10% or more stock interest in the company. You are considered a managing executive if you are authorized without effective veto procedures to decide on the necessity of the trip. You are related to your employer if the employer is your spouse, parent, child, brother, sister, grandparent, or grandchild.

Rule for managing executives and self-employed persons. If you are a managing executive, self-employed, or related to your employer, or have a 10% or more interest, you may deduct all transportation costs if:

1. The trip outside the United States took a week or less, not counting the day you leave the U.S. but counting the day you return,
2. If the trip abroad lasted more than a week, you spent less than 25% of your time, counting the days your trip began and ended, on vacation or other personal activities, *or*
3. In planning the trip you did not place a major emphasis on taking a vacation.

If the vacationing and other personal activities took up 25% or more of your time on a trip lasting more than one week, and you cannot prove that the vacation was a minor consideration in planning the trip, you must *allocate* travel expenses between the time spent on business and on personal affairs. The part allocated to business is deductible; the balance is not. To allocate, count the number of days spent on the trip outside the United States, including the day you leave the U.S. and the day you return. Then divide this total into the number of days on which you had business activities; include days of travel to and from a business destination.

If you vacation at, near or beyond the city in which you do business, the expense subject to allocation is the cost of travel from the place of departure to the business destination and back. For example, you travel from New York to London on business and then vacation in Paris before returning to New York. The expense subject to allocation is the cost of traveling from New York to London and back; see Example 2. However, if from London you vacationed in Dublin before returning to New York, you would allocate the round-trip fare between New York and Dublin and also deduct the difference between that round-trip fare and the fare between New York and London; see Example 3.

EXAMPLES

1. You fly from New York to Paris to attend a business meeting for one day. You spend the next two days sightseeing and then fly back to New York. The entire trip, including two days for travel en route, took five days. The plane fare is deductible. The trip did not exceed one week.
2. You fly from Chicago to New York where you spend six days on business. You then fly to London where you conduct business for two days. You then fly to Paris for a five-day vacation after which you fly back to Chicago. You would not have made the trip except for the business that you had to transact in London. The nine days of travel outside the United States away from home, including two days for travel en route, exceeded a week, and the five days devoted to vacationing were not less than 25% of the total travel time outside the U.S. The two days spent traveling between Chicago and New York, and the six days spent in New York, are not counted in determining whether the travel outside the United States exceeded a week and whether the time devoted to personal activities was less than 25%.

Assume you are unable to prove either that you did not have substantial control over the arrangements of the trip or that an opportunity for taking a personal vacation was not a major consideration in your decision to take the trip. Thus, $\frac{5}{9}$ (five non-business days out of nine days outside the U.S.) of the plane fare from New York to London and from London to New York is not deductible. You may deduct $\frac{4}{9}$ of the New York-to-London round-trip fare, plus lodging, 80% of meals, and other allowable travel costs while in London. No deduction is allowed for any part of the costs of the trip from London to Paris.

3. Same facts as Example 2 except that the vacation is in Dublin, which is closer to the U.S. than London. The allocation is based on the round-trip fare between New York and Dublin. Thus, $\frac{4}{9}$ of the New York to Dublin fare is deductible and $\frac{5}{9}$ is not deductible. Further, the IRS allows a deduction for the excess of the New York-to-London fare over the New York-to-Dublin fare.

Weekends, holidays, and business standby days. If you have business meetings scheduled before and after a weekend or holiday, the days in between the meetings are treated as days spent on business for purposes of the 25% business test just discussed. This is true although you spend the days for sightseeing or other personal

travel. A similar rule applies if you have business meetings on Friday and the next scheduled meeting is the following Tuesday; Saturday through Monday are treated as business days. If your trip is extended over a weekend to take advantage of reduced airfares, the additional expense of meals, lodging, and other incidental expenses is deductible; *see* ¶20.10.

¶20.12 Deducting Expenses of Business Conventions

Conventions and seminars at resort areas usually combine business with pleasure. Therefore, the IRS scrutinizes deductions claimed for attending a business convention where opportunities exist for vacationing. Especially questioned are trips where you are accompanied by your spouse and other members of your family. Foreign conventions are discussed at ¶20.14.

Generally, you may not deduct expenses of attending investment conventions and seminars; *see* ¶19.24. You also may not deduct the costs of business conventions or seminars where you merely receive a videotape of business lectures to be viewed at your convenience and no other business-related activities occur during the event.

In claiming a deduction for convention expenses, be prepared to show that the convention was connected with your business. Cases and IRS rulings have upheld deductions for doctors, lawyers, and dentists attending professional conventions. One case allowed a deduction to a legal secretary for her costs at a secretaries' convention. If you are a delegate to a business convention, make sure you prove you attended to serve primarily your own business interests, not those of the association. However, it is not necessary for you to show that the convention dealt specifically with your job. It is sufficient that attendance at the convention may advance or benefit your position. If you fail to prove business purpose, the IRS will allocate your expenses between the time spent on your business and the time spent as a delegate. You then deduct only the expenses attributed to your business activities.

EXAMPLES

1. An attorney with a general law practice was interested in international law and relations. He was appointed a delegate to represent the American branch of the International Law Association at a convention in Paris. The attorney deducted the cost of the trip and convention as business expenses which the IRS and a court disallowed. He failed to prove that attending the conference on international law helped his general practice. He did not get any business referrals as a result of his attendance at the convention. Nor did he prove the chance of getting potential business from the conference.
2. An insurance agent doing business in Texas attended his company's convention in New York. One morning of the six-day convention was devoted to a business meeting and luncheon; the rest of the time was spent in sightseeing and entertainment.

The company paid for the cost of the trip. The IRS added the reimbursement to the agent's pay and would not let him deduct the amount. The convention in New York served no business purpose. It was merely a method of entertaining company personnel. If there was any valid business to be transacted, the company could have called a meeting in Texas, the area of his home office.

3. A plywood company could not deduct the costs of entertaining 116 customers and employees at a New Orleans hotel during a Superbowl weekend. The company did not reserve conference rooms or make any other arrangements for organized business meetings. The IRS and two federal courts held that although business discussions may have occurred on a random basis, these were secondary to entertainment.

What expenses are deductible? If the convention trip is primarily for business, you may deduct travel costs both to and from the convention, food costs, tips, display expenses (such as sample room costs), and hotel bills. If you entertain business clients or customers, you may deduct these amounts too.

Food and beverage costs are subject to the 50% cost limitation rule as explained in ¶20.24.

EXAMPLE

You attend a business convention held in a coastal resort city primarily for business reasons. During the convention period, you do some local sightseeing, social entertaining, and visiting—all unrelated to your business. You may deduct your traveling expenses to and from the resort, your living expenses at the resort, and other expenses such as business entertaining, sample displays, etc. But you may not deduct the cost of sightseeing, personal entertaining, and social visiting.

Keep records of your payments identifying expenses directly connected with your business dealings at the convention and those which are part of your personal activity, such as sightseeing, social visiting, and entertaining. Recreation costs are not deductible even though a part of your overall convention costs.



Substantiate Convention Business

Keep a copy of the convention program and a record of the business sessions you attend. If the convention provides a sign-in book, sign it. In addition, keep a record of all of your business expenses as explained in ¶20.26.

Fraternal organizations. You may not deduct expenses at conventions held by fraternal organizations, such as the American Legion, Shriners, etc., even though incidental business was carried on. However, delegates to fraternal conventions may in some instances deduct expenses as charitable contributions; *see* ¶14.4.

¶20.13 Travel Expenses of a Spouse or Dependents

Travel costs of a spouse, dependent, or any other individual who accompanies you on a business trip are not deductible unless that person is also your employee and has a bona fide business reason for taking the trip that would justify claiming a deduction if the person took the trip on his or her own.

Even though the travel costs of a non-employee spouse or other person are not deductible, you may deduct the cost of such person's participation in the entertainment of business clients at conventions or business trips if the trip or entertainment meets the tests at ¶20.21. Generally, you may deduct the cost of goodwill entertaining of associates immediately before or after convention business meetings. A convention meeting qualifies as a bona fide business meeting.



How Much To Deduct

If your spouse accompanied you on a business trip, your bills will probably show costs for both of you. These usually are less than twice the cost for a single person. To find what you may deduct where your spouse's presence is for personal and not qualifying business reasons, do not divide the bill in half. Figure what accommodations and transportation would have cost you alone. Only the excess over the single person's costs is not deductible.

EXAMPLE

You and your spouse travel by car to a convention. You pay \$120 a day for a double room. A single room would have cost \$100 a day. Your spouse's presence at the convention was for social reasons. You may deduct the total cost of operating your car to and from the convention city. You may deduct \$100 a day for your room. If you traveled by plane or railroad, you would deduct only your own fare.

¶20.14 Restrictions on Foreign Conventions and Cruises

You may not deduct expenses at a foreign convention outside the North American area unless you satisfy the rules at ¶20.11 and also can show the convention is directly related to your business and it was as reasonable for the meeting to be held outside the North American area as within it.

Apart from the United States, the North American area includes Mexico, Canada, Puerto Rico, U.S. Virgin Islands, American Samoa, Northern Mariana Islands, Guam, Marshall Islands, Micronesia, Palau and U.S. island possessions.

Conventions may also be held in eligible Caribbean countries that agree to exchange certain data with the U.S. and do not discriminate against conventions held in the United States. Barbados, Bermuda, Costa Rica, Dominica, Dominican Republic, Grenada, Guyana, Honduras, Jamaica, Saint Lucia, and Trinidad and Tobago have qualified and are considered to be within the North American area.

Check with the convention operator about whether the country in which your convention is being held has qualified.

Limited cruise ship deduction. Up to \$2,000 a year is allowed for attending cruise ship conventions if all the ports of call are in the U.S. or U.S. possessions and if the ship is registered in the United States. A deduction is allowed only if you attach to your return statements signed by you and by an officer of the convention sponsor that detail the daily schedule of business activities, the number of hours you attended these activities, and the total days of the trip. Do not confuse the \$2,000 limitation with the *per diem* limitation for cruise ship costs discussed at ¶20.5. The *per diem* limitation does not apply to cruises that meet the tests for the up-to-\$2,000 deduction.

Meals and Entertainment Expenses

	See ¶
50% deduction limit	20.15
The restrictive tests for meals and entertainment	20.16
Directly related dining and entertainment	20.17
Goodwill entertainment	20.18
Home entertaining	20.19
Your personal share	20.20
Entertainment costs of spouses	20.21
Entertainment facilities and club dues	20.22
Restrictive test exception for Reimbursements	20.23
50% cost limitation on meals and entertainment	20.24
Business gift deductions are limited	20.25

¶20.15 50% Deduction Limit

You may not deduct the full cost of entertainment for customers or clients at restaurants, country clubs, at home, theaters, and sporting events, even if the expenses qualify under the restrictive tests of ¶20.16. Only 50% of unreimbursed expenses is deductible and this 50% balance is reduced by the 2% AGI floor if you are an employee. Furthermore, all entertainment costs, including meals, must be backed up with records. If you do not keep adequate records, your deductions will be disallowed. The 50% deduction limit for meals and entertainment is discussed at ¶20.24.

¶20.16 The Restrictive Tests for Meals and Entertainment

You must be prepared to show that meal and entertainment costs are ordinary and necessary to your business, and also:

1. Directly related to the active conduct of your business (¶20.17),
or
2. Directly preceding or following a substantial and bona fide business discussion on a subject associated with the active conduct of your business. This test applies to dining and entertainment in which you seek new business or to goodwill entertainment to encourage the continuation of an existing business relationship. Under this test, you may entertain business associates in nonbusiness settings such as restaurants, theaters, sports arenas, and nightclubs, provided the entertainment directly precedes or follows the business discussion. Business associates are: established or prospective customers, clients, suppliers, employees, agents, partners, or professional advisers, whether established or prospective; *see* ¶20.18.

¶20.17 Directly Related Dining and Entertainment

The directly related test limits the deduction of dining and entertainment costs at restaurants, nightclubs, on yachts, at sporting events, on hunting trips, and during social events. If such dining or entertainment fails to meet the directly related tests, it may qualify under the rules discussed in ¶20.18, which require the holding of a business discussion before or after the entertainment.

The directly related test may be met in one of three ways: (1) under the generally related test; (2) as expenses incurred in a clear business setting; or (3) as expenses incurred for services performed.

Generally related test. Under this test, you must show a business motive for the dining or entertainment and business activity during the entertainment. You must show that you had more than a general expectation of getting future income or other specific business benefit (other than goodwill). Although you do not have to prove that income or other business benefit actually resulted from the expense, such evidence will help support your claim. What type of business activity will an IRS agent look for? The agent will seek proof that a business meeting, negotiation, or discussion took place during the period of dining or entertainment. It is not necessary that more time be devoted to business than to entertainment. What if you did not talk business? You must prove that you would have done so except for reasons beyond your control.



Hunting or Fishing Trips

The IRS presumes entertainment during a hunting or fishing trip or on a yacht is not conducive to business discussion or activity. You must prove otherwise.

Clear business setting test. Expenses incurred in a clear business setting meet the directly related test provided also that you had no significant motive for incurring the expenses other than to further your business. Entertainment of people with whom you have no personal or social relationship is usually considered to have occurred in a clear business setting. For example, entertainment of business representatives and civic leaders at the opening of a new hotel or theatrical production to obtain business publicity rather than goodwill is considered to be entertainment in a clear business setting. Also, entertainment which involves a price rebate is considered to have occurred in a clear business setting, as, for example, when a hotel owner provides occasional free dinners at the hotel for a customer who patronizes the hotel.

Costs of a hospitality room displaying company products at a convention are also a directly related expense.

Entertainment occurring under the following circumstances or in the following places is generally not considered as directly related:

- You are not present during the entertainment.
- The distractions are substantial, as at nightclubs, sporting events, or during a social gathering such as a cocktail party.
- You meet with a group which includes persons other than business associates at cocktail lounges, country clubs, golf and athletic clubs, or at vacation resorts.

Services performed test. An expense is directly related if it was directly or indirectly made for the benefit of an individual (other than an employee) either as taxable compensation for services he or she rendered or as a taxable prize or award. The amount of the expense must be reported on an information Form 1099 (unless the amount is less than \$600).

EXAMPLE

A manufacturer provides a vacation trip for retailers whose sales of his products exceed quotas. The value of the vacation is a taxable prize to the retailers. The vacation cost is a directly related entertainment expense for the manufacturer.

¶20.18 Goodwill Entertainment

Goodwill entertaining may qualify as deductible entertainment. Dining and entertainment costs may be deductible if a substantial and *bona fide* business discussion directly preceded or followed the dining or entertainment.

An officially scheduled meeting at a convention is generally considered a bona fide business discussion.

EXAMPLES

1. During the day, you negotiate with a group of business associates. In the evening, you entertain the group and their spouses at a theater and nightclub. The cost of the entertainment is deductible, even though arranged to promote goodwill.
2. In the evening after a business meeting at a convention, you entertain associates or prospective customers and their spouses. You may deduct the entertainment costs.



Scheduling Entertainment and Business Discussions

The business discussion generally must take place the same day as the dining or entertainment. If not, and your deduction is questioned, you must give an acceptable reason for the interval between the discussion and the dining or entertainment. IRS regulations recognize that a day may separate a business meeting and the entertainment of an out-of-town customer. He or she may come to your office to discuss business one day and you provide entertainment the next day, or you provide the entertainment on the first day and discuss business the day after.

The IRS does not estimate how long a business discussion should last. But it does warn that a meeting must involve a discussion or negotiation to obtain income or business benefits. It does not require that more time be devoted to the meeting than to the entertainment.

¶20.19 Home Entertaining

The cost of entertaining business customers or clients at home is deductible provided a business discussion occurs before, during, or after the meal. When you claim such a deduction, be ready to prove that your motive for dining with them was business rather than social. Have a record of the entertainment costs, names of the guests, and their business affiliations.

¶20.20 Your Personal Share

If the entertaining occurred while on a business trip away from home, you deduct your own meal cost as travel expenses away from home. If the entertaining occurred within the locality of your regular place of business, whether you will be allowed a deduction for your share will depend on the agent examining your return. The IRS said in a ruling that an agent will not disallow your deduction of your own part of the meal cost unless he or she finds that you are claiming a substantial amount that includes personal living expenses. In such a case, which generally is limited to situations where personal meals are regularly claimed as part of an “abusive” pattern, the agent will follow the stricter Tax Court rule (sometimes referred to as the “Sutler” rule) and allow only that part of the meal cost that exceeds what you would usually spend on yourself when alone.

¶20.21 Entertainment Costs of Spouses

A deduction is allowed for the spouses’ share of the entertainment costs if they were present during entertainment that qualified as directly related entertainment under the general rule discussed in ¶20.17. For goodwill entertainment, the cost of entertainment of the spouses is deductible if your share and the business associate’s share of the entertainment is deductible. The IRS recognizes that when an out-of-town customer is accompanied by his or her spouse, it may be impracticable to entertain the customer without the spouse. Under such circumstances, the cost of the spouse’s entertainment is deductible if the customer’s entertainment costs are also deductible. Furthermore, if your spouse joined the party because the customer’s spouse was present, the expenses of your spouse are also deductible.

¶20.22 Entertainment Facilities and Club Dues

You may not deduct the expenses of maintaining and operating facilities used to entertain. By law, entertainment facilities are not considered business assets. Examples of entertainment facilities are yachts, hunting lodges, fishing camps, swimming pools, tennis courts, automobiles, airplanes, apartments, hotel suites, or homes in a vacation area. A season box seat or pass at a sporting event or theater is not considered an entertainment facility.

The disallowance rule applies to operating expenses such as rent, utilities and security, and also to depreciation, but not to such expenses as interest, taxes, and casualty losses which are deductible without having to show business purpose.

A deduction may be allowed for expenses such as the cost of food and drinks incurred at an entertainment facility, if they meet the rules of ¶20.16 through ¶20.21.

Club dues. You may not deduct dues for country clubs, golf and athletic clubs, airline clubs, hotel clubs, business luncheon clubs, and other clubs organized for business, pleasure, recreation, or other social purposes. However, IRS regulations generally allow a deduction for dues paid to (1) civic or public service organizations such as Kiwanis, Lions and Rotary clubs; (2) professional organizations such as medical or bar associations; and (3) chambers of commerce, trade associations, business leagues, real estate boards and boards of trade. The deduction for dues is allowed provided that the organization in (1) – (3) does not have a principal purpose of providing entertainment for members or their guests.

¶20.23 Restrictive Test Exception for Reimbursements

As an employer, you can deduct expense allowances or other reimbursements of employee expenses that you treat as compensation and from which you withhold federal tax. You are not subject to the 50% deduction limit; the employee is.

A similar rule applies to meal allowances or reimbursements that you give to an independent contractor and which you report as compensation on Form 1099-MISC where the contractor does not adequately account for the expenses.

The restrictive tests of ¶20.16 do not apply to such reimbursements. They are deductible if they are “ordinary and necessary” business expenses, and you have records to back up the deduction.

¶20.24 50% Cost Limitation on Meals and Entertainment

You may not deduct the full amount of your deductible expenses for business meals and entertainment expenses, such as tickets to sports events. Only 50% of the otherwise allowable amount for food, beverages, and entertainment is deductible.

Taxes and tips are considered part of the cost subject to the 50% limit. If your employer reimburses your expenses, the 50% limit applies to the employer.

The 50% limit applies to both employees and the self-employed. It applies to the \$26, \$30, \$34, or \$38 IRS meal allowance deduction; see ¶20.4. For employee expenses the limit is taken into account on Form 2106 or 2106-EZ (if you are not reimbursed by your employer and do not claim depreciation for a business car), and on Schedule C for self-employment expenses.

EXAMPLES

1. You pay meal and entertainment costs of \$5,000. Only \$2,500 ($\$5,000 \times 50\%$) is considered deductible.
2. Same facts as above, but your employer reimburses your costs after you account for the expenses. His deduction is limited to \$2,500. You have no deduction.

The deductible amount for a ticket treated as an entertainment expense is restricted to the face value of the ticket. Amounts in excess of face value paid to ticket agencies or scalpers are not deductible. The deductible cost of tickets is also subject to the 50% limitation.

EXAMPLE

You buy from a ticket broker five tickets to entertain clients. The face value of the tickets is \$250. You paid \$300 for them. The deductible amount is \$125 ($50\% \times \250).

Exceptions to 50% cost limitation. In the following cases, you may claim a full deduction for meals and entertainment; the 50% limitation does not apply:

1. As an employer, you pay for an employee’s meals and entertainment that is treated as taxable compensation to the employee and as wages for purposes of withholding of income tax.
2. You reimburse an independent contractor for meal and entertainment expenses he or she incurs on your behalf and the contractor does not adequately account for the expenses. You deduct the reimbursements as compensation if they are ordinary and necessary business expenses.
3. As an employer, you incur expenses for recreational, social, or similar activities (including facilities) primarily for the benefit of employees who are not highly compensated employees. For example, the expenses of food, beverages, and entertainment for a company-wide summer party are not subject to the 50% limit.
4. Expenses for meals and entertainment, including the use of facilities made available to the general public, such as a free concert, for advertising or goodwill purposes. For example, the IRS allowed a real-estate broker to fully deduct the cost of free dinners it provided to potential investors who attended its sales presentations. The 50% deduction limitation for meals does not apply to promotional activities that are made available to the general public. The IRS relied on the following example in a 1986 Congressional committee report for purposes of allowing a 100% deduction: A wine merchant provides customers with wine and food to demonstrate the suitability of the wine with certain types of meals. The committee report indicated that the cost of the wine, food, and other costs associated with the wine-tasting function would be fully deductible.
5. Expenses for meals and entertainment sold to the public in your business, such as meal expenses if you run a restaurant, or the cost of providing entertainment if you run a nightclub. These expenses are fully deductible.

6. Food or beverage provided to your employees as a tax-free *de minimis* fringe benefit (¶3.8). This would include expenses of a cafeteria on your premises for employees where meal charges cover the direct operating cost of the cafeteria.
7. The price of tickets to charitable sports events (including amounts in excess of face value) provided the ticket package includes admission to the event. To qualify, a charitable sports event must: (1) be organized for the primary purpose of benefiting a tax-exempt organization; (2) contribute 100% of its net proceeds to such organization; and (3) use volunteers for substantially all work performed in carrying out the event. According to Congressional committee reports, a golf tournament that donates all its proceeds to charity is eligible to qualify under this exception, even if it offers prize money to the golfers who participate or uses paid concessionaires or security personnel. However, tickets to a college football game or similar scholastic events generally do not qualify because they do not satisfy the requirement that substantially all work be performed by volunteers.

The cost of a charitable sports ticket may include seating, parking, and refreshments.

Allocating payment covering lodging and meals. A hotel may include meals in a room charge. In such cases, the room charge must be allocated between the meals, and entertainment and lodging. The amount allocated to meals and entertainment is subject to the 50% cost limitation. If you receive a *per diem* allowance from your employer covering both lodging and meals under an accountable reimbursement plan, you may have to allocate part of the reimbursement to meals in order to deduct expenses in excess of the reimbursement; see ¶20.31.

Skybox rental costs. A skybox is a private luxury seating area at a sports arena. Skybox seats are generally rented for the season or for a series of games such as the World Series. The deductible amount for a rental covering more than one game or performance may not exceed the sum of the face values of non-luxury box seat tickets for the number of seats in the box. The allowable amount is also subject to the 50% cost limitation. Separately stated charges for food or beverage charges at the box are deductible as entertainment expenses and are subject to the 50% cost rule. For example, assume that for two games, you paid \$1,480 for a skybox containing 10 seats—\$740 per game. The cost of 10 non-luxury box seat tickets for each game was \$200, or \$400 total. You may deduct 50% of \$400 non-luxury face value, or \$200. If you had rented the skybox for one game, you could deduct \$370 (50% of \$740) for that skybox because the special limitation applies only where the rental is for more than one game or other performance.

¶20.25 Business Gift Deductions Are Limited

Deductions for gifts to business customers and clients are restricted. Your deduction for gifts is limited to \$25 a person. You and your spouse are treated as one person in figuring this limitation even if you do not file a joint return and even if you have separate business connections with the recipient. The \$25 limitation also applies to partnerships; thus a gift by the partnership to one person may not exceed \$25, regardless of the number of partners.

In figuring the \$25 limitation to each business associate, do not include the following items:

1. A gift of a specialty advertising item which costs \$4 or less on which your name is clearly and permanently imprinted. This exception saves you the trouble of having to keep records of such items as pens, desk sets, plastic bags, and cases on which you have your name imprinted for business promotion.
2. Signs, displays, racks, or other promotional material which is used on business premises by the person to whom you gave the material.
3. Incidental costs of wrapping, insuring, mailing, or delivering the gift. However, the cost of an ornamental basket or container must be included if it has a substantial value in relation to the goods it contains.

If you made a gift to the spouse of a business associate, it is considered as made to the associate. If the spouse has an independent bona fide business connection with you, the gift is not considered as made to the associate unless it is intended for the associate's eventual use.

If you made a gift to a corporation or other business group intended for the personal use of an employee, stockholder, or other owner of the corporation, the gift generally is considered as made to that individual.

Theater or sporting event tickets given to business associates are entertainment, not gift, expenses if you accompany them. If you do not accompany them, you may elect to treat the tickets either as gifts, which are subject to the \$25 limitation, or as entertainment expenses subject to the entertainment expense rules, such as the requirement to show a business conference before or after the entertainment and the 50% cost limitation. You may change your election at any time within the period allowed for tax assessment; see ¶38.5.

Packaged food or drink given to a business associate is a gift if it is to be consumed at a later time.

Gifts not coming within the \$25 limit are: (1) scholarships that are tax free under the rules of ¶12.4; (2) prizes and awards that are tax free under the rule of ¶12.1; (3) gifts to employees, discussed below; and (4) death benefit payments coming within the \$5,000 exclusion prior to its repeal; *see* ¶3.4.

Employee bonuses. Employee bonuses should not be labeled as gifts. An IRS agent examining your records may, with this description, limit the deduction to \$25 unless you can prove the excess over \$25 was pay. By describing the payment as a gift, you are inviting an IRS disallowance of the excess over \$25. This was the experience of an attorney who gave his secretary \$200 at Christmas. The IRS disallowed \$175 of his deduction. The Tax Court refused to reverse the IRS. The attorney could not prove that the payment was for services.

Awards to employees. There is an exception to the \$25 gift deduction limitation for achievement awards of tangible personal property given to your employees in recognition of length of service or safety achievement. Special deduction limits apply to such achievement awards provided they are given as part of a presentation under circumstances indicating that they are not a form of disguised compensation. For example, awards will not qualify if given at the time of annual salary adjustments, or as a substitute for a prior program of cash bonuses, or if awards discriminate on behalf of highly compensated employees.

The amount of your deduction depends on whether the achievement award is considered a qualified plan award. You may deduct up to \$1,600 for all qualified plan awards (safety and length of service) given to the same employee during the taxable year. If the award is not a qualified plan award, the annual deduction ceiling for each employee is \$400. The \$1,600 overall limit applies if the same employee receives some qualified plan awards and some non-qualified awards in the same year.

To be a qualified plan award, the award for length of service or safety achievement must be given under an established written plan or program that does not discriminate in favor of highly compensated employees. The average cost of all awards under the plan for the year (to all employees) must not exceed \$400. In determining this \$400 average cost, awards of nominal value are not to be taken into account. In case of a partnership, the deduction limitation applies to the partnership as well as to each partner.

Safety and length of service. A length of service award is not subject to the rules discussed on the previous page if it is given during the employee's first five years. Furthermore, only one length of service award every five years is considered an employee achievement award.

Safety awards granted to managers, administrators, clerical employees, or professional employees are not considered employee achievement awards. Furthermore, if during the year more than 10% of other employees (not counting managers, administrators, clerical employees, or professional employees) previously received safety awards, none of the later awards are subject to the employee achievement award rules.

Employee's tax. The employer's deductible amount for an employee achievement award is tax free to the employee; *see* ¶3.10. For example, you give a qualified plan award costing \$1,800 to an employee. You may deduct only \$1,600. The employee is not taxed on the award up to \$1,600; the \$200 balance is taxable.

Travel and Entertainment Records

See ¶

Record-keeping requirements	20.26
You need a diary and, generally, receipts	20.27
Reporting T&E expenses as self-employed person	20.28
Reporting T&E expenses where you are not reimbursed	20.29

¶20.26 Record-keeping Requirements

Your testimony—even if accepted by an IRS agent or a judge as truthful—is not sufficient to support a deduction of travel and entertainment expenses. By law, your personal claim must be supported by other evidence such as records or witnesses. The most direct and acceptable way is to have records that meet IRS rules discussed in the following pages. Failure to have adequate records will generally result in an examination of your return and in a disallowance of your travel and entertainment expense deductions. Only in unusual circumstances will evidence other than records provide all of the required details of proof.

If your expenses are reimbursed by your company, you must keep records to support the reimbursement arrangement with your company; *see* ¶20.30.

¶20.27 You Need a Diary and, Generally, Receipts

To satisfy the IRS requirements and to substantiate your claims in the event of an audit, you need two types of records:

1. A diary, account book, or similar record to list the time, place, and business purpose of your travel and entertainment expenses; and
2. Receipts, itemized paid bills, or similar statements for lodging regardless of the amount, and for other expenses of \$75 or more. But note these exceptions:
 - A receipt for transportation expenses of \$75 or more is required only when it is readily obtainable. For example, for air travel receipts are usually provided.
 - A cancelled check by itself is not an acceptable voucher. If you cannot produce a bill or voucher, you may have to present other evidence such as a statement in writing from witnesses to prove business purpose of the expense.

Record-keeping rules for attorneys and other independent contractors who are reimbursed are discussed at ¶20.23.

A receipted bill or voucher must show (1) the amount of the expense; (2) the date the expense was incurred; (3) where the expense was incurred; and (4) the nature of the expense.

A hotel bill must show the name, location, date, and separate amounts for charges such as lodgings, meals, and telephone calls. A receipt for lodging is not needed if its cost is covered by a *per diem* allowance; see ¶20.32.

A restaurant bill must show the restaurant's name and location, the date and amount of the expense, and, when a charge is made for items other than meals or beverages, a description of the charge.

Diary entries. Your diary does not have to duplicate data recorded on a receipt, provided that a notation in the diary is connected to the receipt. You are also not required to record amounts your company pays directly for any ticket or fare. Credit card charges should be recorded.

Your records for entertainment costs must also show (1) the names of those you entertained; (2) the business purpose served by the entertainment; (3) the business relationship between you and your guests; and (4) the place of entertainment. Inattention to these details of substantiation can cost you the deduction. For example, an executive's company treasurer verified that the executive was required to incur entertainment expenses beyond reimbursed amounts. He also kept a cash diary in which he made contemporaneous notes of the amounts he spent. But he failed to note place, purpose, and business relationship. Consequently, there was no record that tied the expenses to his employment and the deduction was disallowed.

You should keep your diary and supporting records for at least three years after the due date for the return which the records support. However, you may not have to keep these records if the information from them is submitted to your company under the rules applied to reimbursed expenses and allowances described at ¶20.30.

Credit cards. Credit card charge statements for traveling and entertainment expenses meet the IRS tests, provided the business purpose of the expense is also shown. Credit card statements provide space for inserting the names of people entertained, their business relationship, the business purpose of the expense, and the portion of the expense to be allocated to business and personal purposes. These statements generally meet the IRS requirements of accounting to your employer for reimbursed expenses (¶20.31), provided a responsible company official reviews them.

EXCUSES FOR INADEQUATE RECORDS

Substantial compliance: If you have made a "good faith" effort to comply with the IRS rules, you will not be penalized if your records do not satisfy every requirement. For example, you would not automatically be denied a deduction merely because you did not keep a receipt.

Accidental destruction of records. If receipts or records are lost through circumstances beyond your control, you may substantiate deductions by reasonable reconstruction of your expenditures.

Exceptional circumstances: If, by reason of the "inherent nature of the situation," you are unable to keep adequate records, you may substantially comply by presenting the next best evidence. A supporting memorandum from your files and a statement from the persons entertained may be an adequate substitute. IRS regulations do not explain the meaning of "inherent nature of the situation."

EXAMPLES

1. Bryan's 1966 records were lost by a moving company. He claimed a T&E deduction of \$15,301.87. The IRS estimated his T&E and other business expenses as \$8,669 on the basis of his 1971 expense records. The Tax Court affirmed the IRS's approach. True, Bryan's loss of records made his burden of proof difficult, but he had to provide a reasonable reconstruction of his records to support his claimed deduction. His testimony of what he incurred in 1966 was not sufficient. A more accurate method was the IRS's use of his 1971 records and receipts.
2. Jackson claimed the IRS lost his records. He left his records with the IRS when he was audited, and the records were never returned. The Tax Court held that to be a good excuse for not producing his records and allowed a deduction on the basis of reconstructed records. Evidence that the IRS lost them: The IRS turned up Jackson's worksheet a year after the audit interview.
3. Murray claimed he lost his records when he was evicted from his apartment for failure to pay rent for a month. The Tax Court accepted his excuse on proof that he had kept records before they were lost. The eviction was beyond his control. However, if the records had been lost during a voluntary move, the loss would not have been excused, as in Example 1.

¶20.28 Reporting T&E Expenses as Self-Employed Person

You must keep travel and entertainment (T&E) records following the rules of ¶20.27. You may claim the meal allowance at ¶20.4 on overnight business trips. The reimbursement rules of ¶20.30 do not apply to you.

In preparing your tax return, you report your expenses on the appropriate lines of Schedule C or Schedule C-EZ (if you qualify). You do not use Form 2106. An advantage of reporting on Schedule C (or C-EZ) is that your travel and entertainment expenses (T&E) are not subject to the 2% adjusted gross income (AGI) floor.

¶20.29 Reporting T&E Expenses Where You Are Not Reimbursed

If you are paid a salary with the understanding that you will pay your own expenses and you pay all of your travel and entertainment (T&E) expenses *without* reimbursement, you report all of your salary or commission income as shown on Form W-2. You report your expenses on Form 2106 or Form 2106-EZ (if other tests are met). Meals and entertainment are only 50% deductible. You must also keep records as required by ¶20.27 to support your deduction. The deductible amount from Form 2106 or Form 2106-EZ is entered on Schedule A as a miscellaneous expense subject to the 2% AGI floor. Therefore, if your total miscellaneous expenses, including the unreimbursed T&E costs, do not exceed 2% of adjusted gross income, none of the miscellaneous expenses will be deductible.

Employer Reimbursement Plans

	<i>See ¶</i>
Tax treatment of reimbursements	20.30
What is an accountable plan?	20.31
<i>Per diem</i> travel allowances under accountable plans	20.32
Automobile mileage allowance	20.33
Reimbursements under non-accountable plans	20.34

¶20.30 Tax Treatment of Reimbursements

Compliance rules are imposed on employees and employers for reporting reimbursed travel and entertainment expenses in order to prevent reimbursement arrangements from being used to avoid the 2% of adjusted gross income (AGI) floor for employee miscellaneous expenses. Plans that allow reimbursements that *do not* comply with the IRS rules are called *nonaccountable plans*. All reimbursements under a nonaccountable plan are reported as salary or wage income on Form W-2. You then deduct your expenses as miscellaneous deductions subject to the 2% AGI floor; *see* ¶20.34.

If a plan meets the IRS rules, the plan is called an *accountable plan* and reimbursements made by the plan are *not* reported on Form W-2 as taxable wages. You also do not have to deduct expenses, assuming the reimbursement equals your expenses. In other words, there is a bookkeeping “wash” in which the full amount of expenses offsets the reimbursement without being reduced by the 2% AGI

floor and in the case of meal and entertainment costs, by the 50% reduction. Even though the employer may only deduct 50% of qualifying meal and entertainment expenses, you are not taxed on any part of a reimbursement of such costs if the accountable plan rules are met.

To qualify a plan as accountable, your employer must see to it that you submit adequate proof of your expenditures, and that you return any excess advances; *see* ¶20.31. To reduce record-keeping for actual costs, the company may reimburse you according to certain fixed *per diem* allowance rates; *see* ¶20.32. Your company must also determine how much of the advance or reimbursement, if any, is to be reported on your Form W-2.

EXAMPLE

Your adjusted gross income is \$85,000, and you incur T&E expenses of \$1,600 which are reimbursed by your company. If the reimbursement arrangement does not meet the IRS rules, the \$1,600 reimbursement is reported as wage income on your Form W-2. You may report the expenses on Form 2106 and claim a deduction on Schedule A as a miscellaneous expense subject to the 2% AGI floor. However, if these are your only miscellaneous expenses, you will not get the benefit of a deduction because they do not exceed 2% of \$85,000, or \$1,700. The \$1,600 is fully taxable although spent for T&E.

If your reimbursement arrangement qualified as an accountable plan, and you made an adequate reporting to your employer, the \$1,600 would not be reported as income on your Form W-2, and you would not have to be concerned with the 2% floor for miscellaneous itemized deductions. There is a bookkeeping “wash.” In other words, you receive a full deduction by substantiating the expenses to your employer.

Reimbursements of club dues or spousal travel costs. If you are reimbursed for nondeductible club dues (¶20.22) or nondeductible travel costs of a spouse or other person (¶20.13), the reimbursement may be treated by your employer as taxable wages. If it is, you are not allowed an offsetting deduction. If the reimbursement is not treated as taxable wages by your employer, and you substantiate a business purpose for the club dues or for a travel companion’s presence, the reimbursement is considered to be a tax-free working condition fringe benefit (¶3.8).

EXAMPLE

A company pays for the country club dues of an executive. In 1996, it reimbursed dues of \$20,000, and the executive used the club for business purposes 40% of the time. If the company does not treat the reimbursement as taxable wages but as a fringe benefit, \$8,000 of the reimbursement is not taxable to the executive; \$12,000 allocated to personal use is taxable.

¶20.31 What Is an Accountable Plan?

A reimbursement or allowance arrangement is an accountable plan if it requires you to:

- Adequately account to your employer for your expenses; *and*
- Return to your employer any excess reimbursement or allowance which you do not show was spent for ordinary and necessary business expenses.

If these terms are met and your expenses are fully reimbursed, you do not report the expenses or the reimbursement on your return. If the reimbursement is less than your payment of expenses, you use Form 2106 and Schedule A to claim a deduction for the unreimbursed expenses. The unreimbursed expenses are subject to the 2% AGI floor on Schedule A.

What is an adequate accounting? You adequately account to your employer by submitting bills and an account book, diary, or similar record in which you entered each expense at or near the time you had it. You must account to your employer for all amounts received as advances, reimbursements, or allowances, including amounts charged on a company credit card. Your records and supporting information must meet the rules of ¶20.27. You must also pay back any reimbursements or allowances for which you do not adequately account or the nonreturned accounts will be taxable under the rules at ¶20.34 for nonaccountable plans.

The accounting requirements are eased if you are reimbursed under a *per diem* arrangement covering meals, lodging, and incidental expenses (¶20.32) or you receive a flat mileage allowance (¶20.33).

If you are entitled to reimbursement from your employer, make sure you ask for reimbursement. Failure to be reimbursed may prevent you from deducting your out-of-pocket expenses. A supervisor whose responsibility was to maintain good relations with his district and store managers entertained them and their families and also distributed gifts among them. His cost was \$2,500 for which he could have been reimbursed by his company, but he made no claim. Consequently, the Tax Court disallowed it as a deduction on his return. The expense was the company's; any goodwill he created benefited it. But because he failed to seek reimbursement, he was not allowed to convert company expenses into his own.

Time limits for receiving advances, substantiating expenses, and returning excess payments. The general rule is that these events must occur within a reasonable time. Under an IRS "safe harbor," the following payments are considered to be within a reasonable time:

- Advance payments—if given to you within 30 days before you reasonably anticipate to pay or incur expenses;
- Substantiation of expenses—if provided to your employer within 60 days after the expense is paid or incurred; and
- Return of excess—if done within 120 days after you pay or incur expenses.

An employer may set up a "periodic statement method" to meet IRS rules. Here, an employer gives each employee periodic statements (at least quarterly) that list the amounts paid in excess of expenses substantiated by the employee and request substantiation of the additional amounts paid, or a return of the excess, within 120 days of the date of the statement. Substantiation or return within the 120-day period satisfies the reasonable time test.

If you fail to return excess payments within a reasonable time but you meet all of the other tests applied to an accountable plan, such as providing proof, only the retained excess is taxed to you as if paid outside of an accountable plan.

Allocating reimbursements to meals and entertainment. Only 50% of meals and entertainment expenses are deductible. Therefore, if you adequately account for your expenses, and receive a flat reimbursement that is partly for meals and entertainment, and partly for other expenses, you must allocate part of the reimbursement to meals and entertainment if the employer has not provided an item-by-item breakdown. You must make this allocation if you want to deduct expenses exceeding reimbursements because on Form 2106, you must separately list meals and entertainment costs and reimbursements for meals and entertainment. The allocation is based on the percentage which your meal costs bear to the total T&E expenses.

EXAMPLE

You receive an allowance of \$1,000 for travel expenses and have total expenses of \$1,500, including \$300 for meals. The percentage of your meals to total expenses is 20% ($300 \div 1,500$). On Form 2106, you show 20% of the allowance or \$200 as the allocable reimbursement for meals. The unreimbursed \$100 balance for meals ($\$300 - \200) must be reduced to \$50 by the 50% reduction for meals. The balance of other travel expenses is \$400 ($\$1,200$ less allocated reimbursement of \$800). The \$450 total is transferred from Form 2106 to Schedule A, where it is deductible as a miscellaneous itemized expense subject to the 2% AGI floor.

¶20.32 Per Diem Travel Allowance Under Accountable Plans

Instead of providing a straight reimbursement for substantiated out-of-pocket travel expenses, an employer may use a *per diem* allowance to cover meals, lodging, and incidental expenses on business trips away from home. Incidental expenses covered by a *per diem* arrangement may include tips, laundry, and cleaning fees, or similar expenses, but, under IRS rules, may not include cab fares, telephone, or telegram costs.

If the *accountable plan* rules (¶20.31) are met and you are not related to the employer, you do not have to give your employer proof of your actual expenses if you receive a *per diem* allowance or reimbursement that is equal to or less than the federal travel rate for the particular area.

For allowances in 1996 covering lodging plus meals and incidental expenses for travel *within* the continental U.S., an employer may use an IRS high-low rate of \$95 for most areas or \$152 per day for “high-cost” areas, instead of the federal travel rate.

Tables published by the government show the federal travel rate for areas within the continental U.S. (called CONUS locations) and for areas outside the continental U.S., including Hawaii and Alaska (called OCONUS locations). The CONUS federal travel rates and IRS high-low rates are in IRS Publication 1542.

If your employer’s method of fixing and reviewing *per diem* arrangements qualifies, you do not have to keep hotel receipts. You do have to account for the time, place, and business purpose of your travel. If you do *not* provide such an accounting for some travel days, you must be required to return the *per diem* allowance received for such days in order for the employer’s plan to qualify.

Employees related to the employer. The IRS *per diem* rules that allow you to avoid accounting for actual expenses do not apply if you work for a brother, sister, spouse, parent, child, grandparent, or grandchild. They also do not apply if you are an employee-stockholder who owns more than 10% of the company’s stock.

Reporting a *per diem* allowance. If the allowance does not exceed the federal travel rate or IRS high-low rate, the reimbursement is not reported on Form W-2. If your expenses do not exceed the reimbursement, you do not have to report the expenses or the reimbursement on your tax return; *see* Example 1 in the next column. If your expenses exceed the allowance, you may deduct the excess by reporting the expenses and reimbursement on Form 2106. The net amount from Form 2106, after applying the 50% reduction for meals, is claimed on Schedule A as a miscellaneous expense subject to the 2% AGI floor; *see* Example 2 in the next column.

Meal allowance only. If your employer gives you a *per diem* allowance covering only meals and incidental expenses, it is not taxable to you if you are not related to the employer and the allowance does not exceed the IRS meal allowance rates under ¶20.4.

For meals *outside* the continental U.S., the meal allowance rates of ¶20.4 do not apply. The allowable meal allowance rates are listed in the government’s OCONUS tables.



Excess Per Diem Allowances

If a *per diem* allowance exceeds the federal travel rate or the IRS high-low rate, the excess will be reported as income on your Form W-2, unless you return the excess or prove to your employer that your actual expenses equal or exceed the allowance; *see* Example 3 below. The excess reportable on Form W-2 is also subject to income tax and FICA tax withholding.

EXAMPLES

1. You take a three-day business trip to a locality at a time when the federal travel rate for the area is \$95 per day. You account for the date, place, and business purpose of the trip. Your employer reimburses you \$95 a day for lodging, meals, and incidental expenses, for a total of \$285. Your actual expenses do not exceed this amount. Your employer does not report the reimbursement on your Form W-2. You do not have to report the reimbursement or deduct any expenses on your return.
2. Same facts as Example 1, except that the reimbursement is less than your actual expenses of \$310 for which you have records. On Form 2106, you report the \$285 reimbursement and your \$310 of expenses. You also must allocate part of the allowance to meals to apply the 50% limit. The net amount from Form 2106 is deductible on Schedule A as a miscellaneous expense subject to the 2% AGI limit.
3. Same facts as Example 1, except that you receive a *per diem* allowance of \$103 per day—\$8 per day more than the federal travel rate. If you do not return the excess of \$24 ($\8×3 days) within a reasonable time (¶20.31), your employer must report the \$24 as income in Box 1 of your Form W-2. The amount up to the federal travel rate, or \$285 will be reported in Box 13 of Form W-2, but not included as income.

¶20.33 Automobile Mileage Allowance

If your employer pays you a fixed mileage allowance of up to 31 cents per mile for 1996, the amount of your automobile expenses is treated as substantiated, provided you show the time, place, and business purpose of your travel. If the allowance is in the form of an advance, it must be given within a reasonable period before the anticipated travel and you must also be required to return within a reasonable period (¶20.31) any portion of the allowance that covers mileage that you have not substantiated.

If these tests are met, the allowance will not be reported as income on Form W-2, and you will not have to report the allowance or expenses on your return; *see* Example 1 in this section. If you do not prove to your employer the time, place, and purpose of your travel the entire reimbursement is treated as paid from a nonaccountable plan and will be reported as income on Form W-2.

If you were given a 1996 mileage allowance in excess of 31 cents per mile, the excess will be included as wages on your Form W-2; *see* Example 2. If your allowance was less than 31 cents per mile, you may deduct the difference as a miscellaneous itemized deduction subject to the 2% AGI floor; *see* Example 3.

Your employer may reimburse you for parking fees and tolls in addition to the mileage allowance.

EXAMPLES

1. You drive 12,000 miles for business and account to your employer for the time, place, and business purpose of each trip. Your employer reimburses you at the IRS rate of 31 cents per mile. None of the reimbursements will be reported as income on your Form W-2, and you do not have to report the reimbursements or any expenses on your return if your expenses do not exceed 31 cents per mile.
2. Same as Example 1 except that you were reimbursed at 32 cents per mile. The amount using the IRS rate, or \$3,720 ($31¢ \times 12,000$ miles), is \$120 less than the reimbursement of \$3,840 ($32¢ \times 12,000$). The \$120 excess over the IRS rate will be reported as wages on your Form W-2.
If you had records substantiating expenses over 31 cents per mile, you could claim them on Form 2106. The excess of your expenses over the IRS rate is shown on Form 2106, and that excess is claimed on Schedule A as a miscellaneous itemized deduction subject to the 2% AGI floor.
3. Same as Example 1 except that you were reimbursed only 20 cents per mile. The reimbursements will not be reported as income on your Form W-2. You may deduct expenses up to the 31-cent IRS rate by reporting the expenses and reimbursements on Form 2106. The amount using the IRS rate, or \$3,720 ($31¢ \times 12,000$ miles), is \$1,320 more than the reimbursement of \$2,400 ($20¢ \times 12,000$). The \$1,320 may be claimed as a miscellaneous itemized deduction on Schedule A subject to the 2% AGI floor.

If you had records showing actual expenses of more than \$3,720, you would claim those expenses on Form 2106 and not use the IRS fixed mileage allowance rate to figure your deduction.

Fixed and variable rate allowance (FAVR). In lieu of setting the allowance at the IRS standard mileage rate (31 cents per mile in 1996), an employer may use a fixed or variable rate allowance, called a FAVR, that gives employees a cents-per-mile rate to cover gas and other operating costs, plus a flat amount to cover fixed costs such as depreciation, insurance and registration. A FAVR allowance must reflect local driving costs and allows employers to set reimbursements at a rate that more closely approximates employee expenses. If your employer sets up a qualifying FAVR under IRS guidelines, you will be required to provide records substantiating your mileage and certain car ownership information. Expenses up to the FAVR limits are deemed substantiated and will not be reported as wages on your Form W-2.

¶20.34 Reimbursements Under Non-Accountable Plans

A non-accountable plan is one that either does not require you to adequately account for your expenses, or allows you to keep any excess reimbursement or allowances over the expenses for which you did adequately account.

Your employer reports allowances or reimbursements for a non-accountable plan as part of your salary income in Box 1 of your Form W-2. The allowance is also subject to income tax and FICA tax (Social Security) withholding. To claim deductions, you must use Form 2106 and itemize your deductions on Schedule A. Your expenses are subject to the 2% AGI floor.

Important: If you adequately report expenses to your employer and return excess reimbursements, you are treated as being reimbursed under an accountable plan and generally do not have to report any reimbursement on your return; see ¶20.31.

